CITY OF CAPE TOWN
ISIXEKO SASEKAPA
STAD KAAPSTAD

ANNEXURE 17

POLICY GOVERNING PLANNING AND APPROVAL OF CAPITAL PROJECTS

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1. DEFINITIONS AND ABBREVIATIONS

ABBREVIATIONS

DORA - Division of Revenue Act

MBRR - Municipal Budget and Reporting Regulations

MFMA - Local Government Municipal Finance Management Act No. 56 of 2003

DEFINITIONS

Accounting Officer- (MFMA) in relation to a municipality, means the municipal official referred to in section 60". The municipal manager of a municipality is the accounting officer of the municipality for the purpose of this Act.

Annual Division of Revenue Act (DORA) – (MFMA) means the Act of Parliament, which must be enacted annually in terms of section 214 (1) of the Constitution.

Approved budget (MFMA) means an annual budget-

(a) approved by a municipal council, or

(b) approved by a provincial or the national executive following an intervention in terms of section 139 of the Constitution, and includes such an annual budget as revised by an adjustments budget in terms of section 28.

Budget Year – (MFMA) means the financial year for which an annual budget is to be approved in terms of section 16 (1).

Financial Year – (MFMA) means a year ending 30 June.

Municipal Council or **council** – (MFMA) means the council of a municipality referred to in section 18 of the Municipal Structures Act.

Municipality – (MFMA)

(a) when referred to as a corporate body, means a municipality as described in section 2 of the Municipal Systems Act; or

(b) when referred to as a geographic area, means a municipal area determined in terms of the Local Government: Municipal Demarcation Act, 1998 (Act No. 27 of 1998);

National Treasury – (MFMA) means National Treasury established by section 5 of the Public Finance Management Act.

2. PURPOSE

2.1 This policy aims to provide guidelines through which Directorates can plan and obtain approval of projects of a capital nature.

2.2 This policy is required - in terms of regulation 7 of the Local Government: Municipal Budget and Reporting Regulations (MBRR).

3. PROBLEM STATEMENT

The Act replaced the current antiquated system of local government finance inherited from the previous rules-bound dispensation in 1994, which focused on rules and procedures rather than on sound outcomes. These practices included one-year, detailed line-item budgets, which did not allow for forward-planning or long-term strategic planning. Previous practices were one dimensional, financial processes that were generally centrally controlled by prescribed bureaucratic rules and regulations that stifled managerial efficiency, inhibiting innovation and information and often resulting in poor decision-making and a passive approach to financial management generally.

Financial planning within municipalities tended toward short-term outputs that were not necessarily integrated into long-term outcomes. Budgets typically catered for immediate demands with little or no view to future needs or the future consequences of particular decisions.

4. DESIRED OUTCOMES

The Municipal Finance Management Act (MFMA), No.56 of 2003 aims to modernise budget and financial management practices in municipalities in order to maximise the capacity of the municipalities to deliver services to all their residents, customers and users. It also gives effect to the principle of transparency as required by sections 215 and 216 of the Constitution.

The MFMA therefore supplements conventional procedural rules with a performance- based system focusing on outputs and measurable objectives, to enable municipalities to maximise their capacity for service delivery.

The MFMA empowers councilors to play their constitutional role as politically elected representatives of the community and residents by approving policies and budgets proposed by the executive mayor or committee and then overseeing the performance of the municipality in implementing these policies and budgets.

All these various roles are possible only because of the reporting requirements of the MFMA, as the Act recognises that effective service delivery is possible only with good-quality and timely management information. Such information allows management to be proactive, identifying and solving problems as they arise. The challenge facing all stakeholders is their capacity to use the information produced in terms of the MFMA to improve the efficiency and effectiveness of the service delivery of the municipality.

5. ROLE PLAYERS AND STAKEHOLDERS

In order to implement and give effect to the approved Capital budget the relevant role players and their respective powers, duties and responsibilities are listed below:

5.1 Budgets Department

(a) be responsible for administrative and technical guidance in terms of the compilation of the Capital Budget.

(b) review this policy, in consultation with relevant stakeholders, to ensure maximum compliance in terms of legislation.

5.2 Directorates and Departments:

(a) in consultation with their relevant Executive Director, MayCo Member and Portfolio committee are required to inform the Budgets Department of their proposed budget.

5.3 Council

Responsible for the approval of the Capital Budget.

6. STRATEGIC FOCUS AREAS

The **five** strategic focus areas provide a solid foundation for service delivery. The strategic focus areas are the opportunity city, the safe city, the caring city and the well-run city.

The City has also identified **11 priorities** that span the five strategic focus areas. By elevating these 11 priorities, it is expected that the strategic focus area outcomes will be accelerated.

This policy supports the following strategic focus area:

Well-run City: This objective is about delivering services and creating value for customers in an operationally sustainable manner based on evidenced led decision making so that the City can remain financially stable and resilient to shocks in a changing environment.

Objective 5.1: Operational sustainability.

7. REGULATORY CONTEXT

This policy must be read, analysed, interpreted, implemented and understood against this legislative background. The budget plays a critical role in an attempt to realise diverse community needs taking into account the IDP process. The formulation of a municipal budget should also take into account the government's macro- economic and fiscal policy fundamentals.

In terms of the MFMA, Chapter 4 on Municipal Budgets, section 16, states that "the council of a municipality must for each financial year approve an annual budget for the municipality before commencement of that financial year. According to section 16(2), in order to comply with section 16(1), the executive mayor of the municipality must table the annual budget at a council meeting at least 90 days or earlier before the start of the budget year.

Section 18 of the MFMA which relates to Funding of expenditure states that

18. (1) An annual budget may only be funded from-

(a) realistically anticipated revenues to be collected;

(b) cash-backed accumulated funds from previous years' surpluses not committed for other purposes; and

(c) borrowed funds, but only for the capital budget referred to in section 17(2).

(2) Revenue projections in the budget must be realistic, taking into account-

(a) projected revenue for the current year based on collection levels to date; and

(b) actual revenue collected in previous financial years.

Section 19 of the MFMA states that for Capital projects –

(1) A municipality may spend money on a capital project only if –

(a) the money for the project, excluding the cost of feasibility studies conducted by or on behalf of the municipality, has been appropriated in the capital budget referred to section 17(2);

(b) the project, including the total cost, has been approved by the council;

(c) Section 33 has been complied with, to the extent that that section may be applicable to the project; and

(d) the sources of funding have been considered, are available and have not been committed for other purposes.

(2) Before approving a capital project in terms of subsection (1) (b), the council of a municipality must consider -

(a) the total projected cost covering all financial years until the project is operational; and

(b) the future operational costs and revenue on the project, including municipal tax and tariff applications.

(3) A municipal council may in terms of section19 (1) (b) approve capital projects below a prescribed value either individually or as part of consolidated capital programme.

Regulation 13 of the MBRR on the approval of capital project[1] states that:

(1) Within ten working days after the municipal council has given individual approval for a capital project in terms of section 19(1)(b) of the Act, the municipal manager must in accordance with section 21A of the Municipal Systems Act make public-

(a) The municipal council resolution approving the capital project; and

(b) Details of the nature, location and total projected cost of the approved capital project.

[1]The MFMA must be read in conjunction with the Municipal Budgeting and Reporting Regulations (MBRR) as it provides further clarity on matters that are prescribed in the MFMA. Section 19 of the MFMA regulates budgetary matters in relation to capital projects. In terms of section 19(1)(b) a municipality may not spend any money on a capital project unless the council has approved the specific project including the total cost. Section19 (3), however, provides that capital projects below a prescribed value may be approved either individually or as part of a consolidated capital programme.

(2) The following capital projects may be approved by council either individually or as part of a consolidated capital programme as contemplated in section 19(3) of the Act:

(c)Capital projects of which the total projected cost is below R50 million, in the case of a municipality with approved total revenue in its current annual budget greater than R500 million[2].

(3) Subregulation (1) does not apply to capital project whose total projected cost when the annual budget is approved is below the values set out in subregulation (2).

(4) Expenditure needed for capital projects below the values set out in subregulation (2) may be included in the annual budget before the project is approved in terms of section 19(3) of the Act.

8. CAPITAL BUDGET

The City of Cape Town's (the City) Capital Budget is compiled, amended and maintained in accordance to:

(a) Generally Recognised Accounting Practice (GRAP) principles and statements;
(b) Relevant legislations: e.g. MFMA and chapter 4 of System Act;
(c) National Treasury – MFMA circulars and budget regulations;
(d) Division of Revenue Bill/Act (DORA);
(e) The City's Asset Management policy;
(f) The Integrated Development Plan (IDP); and any other City strategies and frameworks

9. BASIS OF CAPITAL BUDGET

(a) The zero based method is used when proposing new capital projects, except in cases where a contractual commitment has been made that would span over more than one financial year.
(b) All capital projects must be funded from realistically anticipated revenue.
(c) No capital project will be accepted for inclusion into the capital budget unless it is accompanied by the total project cost and operating impact covering all financial years the project is operational and a cash flow for the project.

[2]Capital projects of which the total projected cost is above these values must be approved individually by the council in terms of section 19(1)(b) of the Act

(d) The consequence of the operating impacts should be carefully analysed by Directorates when proposing a new capital project for inclusion on an annual budget, such impacts includes finance charges to be incurred on external loans, depreciation of the fixed asset, maintenance on fixed assets and any other operating expenditure.

(e) In addition, the Council must consider the likely impact of such operational expenses on future property rates and service tariffs.

(f) Expenditure of a project shall be included in the capital budget: if it is probable that future economic benefits or service potential associated with the asset will flow to the municipality; the cost or fair value of the asset to the municipality can be measured.

(g) The budget approved by Council for assets shall clearly distinguish between enhancement, replacement and new assets.

(h) A municipality may spend money on a capital approval object only if the money for the project has been appropriated in the capital budget.

(i) The envisaged sources of funding for the capital budget must be properly considered and the Council must be satisfied that this funding is available and not been committed for other purposes.

(j) Carry-over of capital projects from the previous year will be considered for inclusion if they fall within the existing levels of the Capital Budget. Directorates must identify carry – over budget requests during the mid-year review and adjustments process.

(k) New or additional projects (excluding Ward Allocations projects) included in the proposed Capital Budget which were not previously approved by Council must be fully supported by the relevant Mayoral Committee Member and Executive Director and not prejudice any committed projects.

(l) The proposed Capital Budget and Capital Programme which is submitted to the Budgets Department by the Directorates must by aligned to the IDP and any other special policy decision.

(m) The City adopted the programme budgeting methodology

10. FUNDING A MUNICIPAL CAPITAL BUDGET

In terms of the MFMA section 18: A fundamental element to planning is the funding of the proposed project that was identified. Budget should be funded accordance to section 18 of the MFMA.

11. SOURCES OF FUNDING

11.1. Revenue

(a) If the project is to be financed from surplus funds, then there must be sufficient cash available for the implementation of the project.

11.2. External Financing Fund (EFF)

External Financing Fund (EFF) is the borrowed component (loans) of capital funding, which is linked to the life expectancy of the asset. In the case of the City it is linked to the City's borrowing programme and earmarked for long-term use.

(a) External loans can be raised only if it is linked to the financing of an asset.

11.3. Capital Replacement Reserve (CRR)

(a) Council shall establish a CRR for the purpose of financing capital projects and for the acquisition of assets. Such reserve shall be established from the following sources of revenue:
   i. Unappropriated cash-backed surpluses to the extent that such surpluses are not required for operational purposes;
   ii. Interest on the investments of the CRR, appropriated in terms of the investments policy;
   iii. Additional amounts appropriated as contributions in each annual or adjustments budget; and

(b) Before any asset can be financed from the CRR the financing must be available within the reserve and available as cash as this fund must be cash backed;

(c) If there is insufficient cash available to fund the CRR, this reserve fund must then be adjusted to equal the available cash.

11.4. Grant Funding

Government grants as well as private sector funds - Municipalities receive National Treasury and Provincial Treasury allocations. These grants are approved and published in the Division of the Revenue Act (DORA) and Western Cape Government gazette respectively and should be included in Municipal Capital Budget programme. All projects funded externally must be linked to a Grant Fund (GD).

(a) Capital expenditure must be budgeted for in the capital budget;
   i. Interest earned on investments of Conditional Grant Funding shall be capitalised if the condition stated the interest accumulate in the fund.
   ii. If there is no condition stated, the interest can then be allocated directly to the revenue accounts.
   iii. Grant funding should be secured by way of a legal binding agreement, before spending can take place.

Donations and public contributions - Local and foreign donors may sometimes donate a capital funds to be used specifically for the purchase of a capital item.

11.5. Other Funding Sources

Contributed assets:

All physical Assets that are expected to be given to the City should be identified early and their fair value settled to the Asset register (capitalised) in a similar manner to existing Capital projects. A capital asset donated by external parties requires from the directorate to submit a report in order to obtain permission from Council to accept the donation of capital items. Council approves the acceptance of the physical asset after considering specifications and future cost of operating and maintaining the asset.

Public/Private Partnerships:

Capital costs can be paid for by means of partnerships between the private sector and the municipality. The process to follow regarding Public/Private Partnerships remains within the policy governing planning and approval of capital projects.

12. IMPLEMENTATION, EVALUATION AND REVIEW

(a) This policy shall be implemented once approved by Council.
(b) This policy must be reviewed on an annual basis.
(c) Changes in legislation must be taken into account for future amendments to this policy.
(d) Any amendments to the policy must be submitted to Council for approval.